THE PHILOSOPHY AND LIMITATIONS OF SOCIAL ACCOUNTING

BY

LIN SUNG CHIAO

B.S., National Shanghai Institute of Commerce, 1942
M.S., University of Illinois, 1948

AN ABSTRACT OF A THESIS

SUBMITTED IN PARTIAL FULFILLMENT OF THE REQUIREMENTS
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THE PHILOSOPHY AND LIMITATIONS OF SOCIAL ACCOUNTING

Statistics for national income have long been regarded as good indicators of the economic activities of a country. Recent years have seen a great advance in national income studies, conceptual as well as technical. One aspect of the advance which strikes us most is the increasing importance of the accounting approach to national economic analysis through national income concepts. After World War II several systems, more or less similar in nature, in this direction have been devised and applied in various countries.

Most statisticians and economists working in the field of national income recently declared that their statistics are largely based on accounting data and are classified, cumulated and presented in general accordance with enterprise accounting concepts and techniques. As a result, they often call their procedures and efforts "social accounting" or "national income accounting." The term "social accounting," in this study, therefore refers to the asserted application of accounting concepts and techniques to the collection, compilation, and presentation of the aggregate and the constituent data of the income of a national economy.

It is not the purpose of this work to develop or formulate a new system of social accounting. It is the objective rather to evaluate the systems as they already exist. Evaluation, however, may be undertaken by two different tests. Firstly, does social accounting aid our understanding of economic change; i. e., does social accounting provide more essential information about the functioning of the national economy than ordinary national income estimates do? Secondly, does social accounting come within the conceptual and technical requirements of private enterprise accounting; i. e., does social accounting conform to the concepts and techniques of conventional enterprise accrual accounting?

The first test deals with the merits and demerits of the social accounting system itself and has been extensively discussed in various national income and social accounting publications. From the professional accounting point of view it is far more important to search for the reasoning or lack of reasoning for applying accounting concepts and techniques in the compilation of aggregate data of a national economy in a social accounting system which has been thus far carried out almost solely by econometricians. Thus, the problems discussed are mainly of an accounting nature, though they would be relevant in terms of the broader economic considerations.

Social Accounting — A Statistical Expediency

To its original exponents, the subject matter of social accounting is unquestionably economic in character, yet, its basic methodology seems that of accounting. In terms of economic concepts social accounting may be perfectly and suitably used as a tool for national income analysis. By means of some features of accounting methodology social accounting may also supply data under verifiable objectivity in its quantitative measurement. However, under thorough investigation, social accounting is a compromise between the two; yet it is neither wholly economics nor fully accounting. It possesses neither accounting certainty nor economic suitability; it serves only as a statistical expediency. It possesses no accounting certainty because it brings imputation, estimation, and sampling into its computation, and the accounting type of dependability is thereby sacrificed. It possesses no economic suitability because it disregards several economic attributes, such as change of taste and quality; and conceptual perfection is violated.

Being partly true to economics and partly true to accounting, social accounting is not accounting enough to include all of accounting or economic enough to coincide with economics. It is not accounting enough because there are many accounting truthfinding methods outside of the social accounting system. Take the utilization of double-entry mechanism for example.

Double-entry bookkeeping not only means the doubleness of entry in debit and credit sides of two accounts but more importantly means the integration of real accounts and nominal accounts. Social accounting includes only the less important one, the "doubleness," but excludes the more important one, the "integration."

It is not economic enough because there is much economic truth outside of the social accounting system. Some national income concepts carried in social accounting are not in complete conformity with economic concepts. The social accountant frequently accepts a concept which is less than ideal in order to achieve a significance not attainable by an immeasurable concept. Conceptually national income should include all economic activities that exist within a nation. To mention only one example, that due to the extreme difficulty of estimates, a great bulk of economic activity, such as work done by housewives, spare time jobs, etc., is excluded from the national income calculations; yet these belong in the economic concept of income.

Limited Applicability of Accounting Concepts

Accounting has a wide serviceability but it is not an unlimited one. In the discussion of accounting function there is always a tendency to confuse central purpose with possible uses. The uses to which accounting may be put are many and diverse; nevertheless, concepts and techniques cannot be oriented equally well to all possible uses, nor can each use have its own set of concepts and techniques. It is obvious that accounting serves several purposes. If some of these purposes are in conflict, and accounting is pulled one way by one interest and another by a second, then accounting is not consistently in accord with a single coordinated body of theory. Yet accounting is actually built within a single coordinated body of theory that preserves its individual characteristics. In this body of theory there are numerous definite and basic concepts and procedures that make accounting different from all other methods of quantitative analysis.

Business enterprise accounting supplies dependable and relevant information about a particular enterprise alone. Business enterprise is primarily interested in maximizing its profit and accounting is mainly used to compute this profitability. In its periodical income determination accounting always relates net profit earned to proprietorship capital employed. For the purpose of objectivity and dependability accounting always depends upon bargained transactions between two independent parties and it assumes the stability of monetary value.

It is obvious that these concepts can hardly be applied to national income estimates for they are taken from a different point of view. From the viewpoint of a large society social accounting seeks data to measure the level of employment. Emphasizing the real productivity social accounting attributes income to all productive processes (not necessarily by realization) and makes adjustments for changes in the purchasing power of money (assumes the changing value of money).

The accepted concepts in accounting have a practical view which is conditioned by a commitment of acounting to serve the data needs of the management of an individual business enterprise. Social accounting, on the other hand, is concerned with logically related larger ideas and with thoughts about attaining a better society. Accounting is in its very essence practical whereas national economy is scarcely within the realm of practice. If accounting were to aspire to become as theoretical as economics, it would have to sacrifice a good deal of its present essence — objectivity. If social accounting were to aspire to become as practical as accounting, it would have to loosen its ties to social objectives.

While business income accounting and national income accounting seem to speak the same language they work with fundamentally different concepts. The failure to recognize these differences would lead to social accounting practices that tend to defeat the purpose for which its accounts are kept, and social accounting will thus never serve its right purpose. To

ignore actual differences because of apparent similarities of method is often the cause of discord among people of influence in the formulation and conduct of important national economic policies.

Effect on Accounting Concepts

Through the investigation it became obvious that social accounting does not quite come within the conceptual requirement of enterprise accrual accounting. Then a collateral question might reasonably airse. Will the development of social accounting tend to react upon enterprise accounting in ways that may profoundly change the concepts and practices of the latter? It appears unlikely. It is true that a change or modification in established accounting concepts would produce different data of much assistance to the work of making national income estimates, and social accounting might then have easier ways of making its measurements of the whole economy. However, it is also true that with a change of accounting concepts it would become necessary to ask enterprise accounting to give up some of its enterprise service.

It is desirable to support any attempt of making accounting data more serviceable in a new field. However, it would be a bad practice to reduce at the same time its serviceability in an area where accounting has been rendering service for a long time. Such a result would hardly be progress.

It is true that the change of basis of depreciation from historical cost to replacement cost, for example, may ease the work of the social accountant. This is true because the social accountant is concerned to face the real issues and places the emphasis on the adequacy of depreciation or replacement fund rather than on the spreading of prior historical costs through amortization. To him, if increased costs of replacing assets are not provided for, the nation is counting capital consumption as part of its current income and distributing it. He believes that neither national income nor net capital formation is measured accurately if depreciation is based on historical cost.

However, it is also true that change of depreciation basis would cause accounting to lose a great deal of its serviceability in business enterprises. It would lead to erroneous interpretation of the efficiency and capability of management of a private business in employing capital with satisfactory foresight in the face of the pressure of competition. The essence of depreciation accounting in business has been to spread or amortize the original cost of an asset over its useful life. This is true because money cost of the asset acquired is the only proper basis of the charge against periodic income, and invested cost is the only objective data identifiable with prior decisions of management. If aid is given social accounting in presenting data of national economy it should not be at the price of clouding the picture of facts about a given enterpirse for people interested in that enterprise.

Moreover, the change of accounting to make possible a more satisfactory measurement of national income might also cause business accounting to be legally unacceptable. Business enterprise is conducted exclusively within the limits set by laws and commercial customs of the time and place. National economy, on the contrary, has less legal restriction. Contractual relationships between debtors and creditors which are an important consideration in business accounting have no place in social accounting. The transfer of ownership of existing assets, used cars for example, has important effect in business accounting but does not have any meaning in measuring the level of national economic activities. The bad result of enterprise accounting will come if the contractual relationship of debtors and creditors has to be taken out of accounting action.

Participation of Accountants Desired

In spite of the fact that the change of accepted accounting concepts to fit the need of social accounting seems undesirable, this, however, does not mean that accountants may not participate in the work of national income estimates, thus allowing econometricians or others to appropriate accounting's tools and make inadequate or even misuse them in social

accounting.

Instead of being adversely critical of the attempts to use accounting by social accountants, this writer sees the urgent need of accountant's participation, in a team, with the work of social accountants. It is hoped that the potentialities of accounting will occur; however, only if accountants can be persuaded to take a part in the development of social accounting. Accountants are therefore urgently needed in the teamwork of national income compilation.

To date, social accounting has been worked out almost entirely without the participation from the accountant. The double-entry system is uesd either incorrectly or incompletely by the econometricians. And balance sheet items are almost entirely missing from the present form of social accounting. If accountants had participated in social accounting not only the integration of real accounts and nominal accounts might have been possible and also a national balance sheet and statement of source and application of funds might have already been made. This is reasonable because integration of real accounts and nominal accounts is the central theme of the double entry system and to an accountant the idea of a national balance sheet seems a logical corollary of the idea of a national income statement.

Moreover, by the accountant's participation in social accounting the distinctions between economic concepts and accounting concepts will be brought into direct contact. Economics and accounting have grown up, as they did, side by side, yet without much interchange. It has long been hoped that there will be a time of better understanding and mutually profitable interchange of ideas by accountants and economists. Social accounting, if there is one at all, is surely a meeting ground of the accountant and the economist. From here there will be a better understanding and closer cooperation between economists and accountants — a closer relationship which they have not had. It is at this point that economists and accountants seem to attain their closest point of proximity. Both accountants and economists should understand both their

limitations and implications. The fact that accountants deal with costs rather than values will be made clear to economists. While the study made herein does not indicate the possibility of any basic modification of current accounting concepts, it shows very clearly the need of the accountant's participation in the teamwork of social accounting.

VITA

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